



**APPROVED MINUTES**  
**APPROVED 03-21-11**

**CITY OF SCOTTSDALE  
AUDIT COMMITTEE**

**MONDAY, JANUARY 24, 2011**

**CITY HALL  
KIVA CONFERENCE ROOM  
3939 NORTH DRINKWATER BOULEVARD  
SCOTTSDALE, AZ 85251**

**REGULAR MEETING**

**PRESENT:** Councilman Robert Littlefield, Chair  
Councilwoman Lisa Borowsky (arrived 4:05 p.m.)  
Vice Mayor Suzanne Klapp

**STAFF:** Phil Montalvo, Administrative Services  
David Smith, City Treasurer  
Anna Henthorn, Finance & Accounting  
Jeff Nichols, Finance & Accounting  
Steve Randall, Fire Department  
Bernadette LaMazza, Human Resources  
Velicia McMillan, Human Resources  
Terry Welker, Human Resources  
Brad Hartig, Information Systems  
John Cocca, Police Department  
Marshall Brown, Water Resources  
Kyla Anderson, City Auditor's Office  
Joyce Gilbride, City Auditor's Office  
Lisa Gurtler, City Auditor's Office  
Sharron Walker, City Auditor's Office

## **CALL TO ORDER**

Chair Littlefield called the meeting to order at 4:04 p.m.

### **1. Approval of Minutes, Regular Meeting, November 15, 2010**

Vice Mayor Klapp moved to approve the minutes of the November 15, 2010 Regular Meeting. The motion carried by a vote of two (2) to zero (0). Councilwoman Borowsky was not yet present.

### **2. Discussion and possible direction to staff regarding Audit Report No. 1104, Selected Application Controls over the City's Total HR System**

Ms. Joyce Gilbride said the objective of this audit was to review the application level controls for the City's TotalHR system. The application controls help ensure the proper operation of specific applications. The TotalHR application maintains employee information such as pay and benefits, and processes payroll. It is supported primarily by a technology group in Finance and Accounting who process payroll and system changes. The HR Division also plays a role by entering new employee benefit selections and other information.

Auditors assessed the effectiveness of system access controls by reviewing appropriateness of access levels based on job function. They looked for proper segregation of duties and assessed the effectiveness of change management controls by reviewing the test environment and a sample of the most recent system changes. They also assessed the effectiveness of security management controls by reviewing systems security parameters such as password requirements.

The auditors found that generally controls were sufficient. TotalHR is an established application used by experienced staff. However, possibly due to staff's level of experience, some of the processes and documentation are less formal than they should be. The audit recommends a review of current user access, a segregation of duties analysis, improving change management documentation, and some improvements to system security.

Vice Mayor Klapp inquired whether TotalHR will be upgraded soon. Mr. Brad Hartig of Information Systems said the audit recommends reviewing possible changes to the security parameters, but not replacing the system, which is working very well. Mr. Terry Welker of Human Resources said there is a slightly more robust system, PeopleAdmin, but it is much more costly. He elaborated that currently HR is using three completely independent systems, TotalHR, a system for new applicants, and a documents management system. PeopleAdmin will be coming back to the City within the next three to four months with a proposal.

Chair Littlefield said if the department were to switch systems the cost of conversion would have to be factored in. Mr. Welker said the current systems are functioning at a high level with good controls in place. There is not really a reason to replace TotalHR.

Chair Littlefield said the problems noted in the audit can all be fixed within the current system.

Mr. Hartig added that even though an eager vendor has approached the City, policy requires that they would have to seek competitive bids if considering a change.

Chair Littlefield confirmed that everyone involved was on board with the suggestions in the audit report.

### **3. Discussion and possible direction to staff regarding Audit Report No. 1007, Overtime Practices and Controls**

Ms. Gilbride stated the audit evaluated department controls established for managing overtime and reviewed activities and trends for the past few years. Although overtime pay has been a significant expenditure for many years, there has been a downward trend in costs over the past few years. The audit found that generally overtime hours and pay are in compliance with City policies, properly approved and substantiated.

However the audit noted high levels of overtime incurred by the same employees in multiple years. Some employees also exceeded the annual limits set for overtime hours, although this has diminished considerably since FY 2007/08. Some overtime is inherent due to the nature of the job. However the audit recommended that management review individuals' high overtime balances to see whether duties can be shifted or if additional staff is needed to avoid overworking certain employees.

The auditors also found that some employees in positions not normally eligible for overtime are receiving additional pay for working beyond normally scheduled hours, which is being paid at straight time rather than time and a half. City Code allows premium pay under extraordinary circumstances or emergency conditions, upon approval of the City Manager. However, the situations found were recurring staffing requirements rather than emergency situations. The auditors recommended Human Resources evaluate these situations to determine whether they are reasonable and meet the City Code requirements for premium pay.

Finally, some overtime policies can be updated. An annual limit for overtime hours for the Fire Department has not been formally documented, and the auditors recommend that Department and HR work together to establish what it should be. They also recommend updates to AR 354, *Overtime Management and Utilization*, for consistency and compliance with the Fair Labor Standards Act. Ms. Gilbride noted that representatives from the Police, Fire, and Water Departments were in attendance, as well as HR staff.

Assistant Chief John Cocca of the Police Department said the Department is in agreement with the findings of the report. He added that the employees whose overtime has been high in the past will continue to be high because of their specialty. Most are related to technology, surveillance, and SWAT. The Department has succeeded in reducing the annual overtime budget by over \$3 million over the last few years. Being fully staffed has helped to reduce overtime.

Steve Randall of the Fire Department said there are many reasons why their staff works overtime. The Department has many controls in place to keep overtime on budget and in compliance with the FLSA. They will be working with HR on the issues identified. The Department adopted the 25 percent overtime rule that is used by the Police Department but this was never formalized in City policy.

Mr. Marshall Brown of the Water Department said he appreciated the audit, and he expects overtime to continue to decrease.

Vice Mayor Klapp said she felt that overtime of exempt employees should be reviewed more frequently.

Mr. Welker responded that department directors would monitor this with the payroll cycles and bring any issues to HR's attention immediately. At the same time, HR would ask directors for explanations if HR sees anything unusual.

Vice Mayor Klapp said that is fine as long as department heads are taking this matter seriously.

Mr. Welker elaborated that in discussions with the departments, HR did not want to take on the role of "the overtime police." He stated that in the audit, the Fire Department was the only Department found to be paying overtime to exempt employees. City Auditor Sharron Walker clarified that Public Works also does this sometimes. Mr. Welker said he saw the role of HR as gathering the information on an annual basis in order to compare the departments for consistency.

Chair Littlefield said this sounds reasonable but they need to ensure that departments are not violating the City's own administrative regulations. He asked who will fix that. Mr. Welker said HR will monitor for compliance at least annually and more frequently if necessary. Mr. Welker said HR will take the lead to modify AR 354. This regulation was last updated before the Fire Department was created.

Vice Mayor Klapp stated that since the policy is that overtime for exempt employees is supposed to be approved by the City Manager, HR should be monitoring this closely and investigating any deviations from policy.

Ms. Walker clarified that the City Manager has been approving this overtime. But the policy says that this can only take place in emergencies or when there are extraordinary circumstances.

Mr. Welker said HR will meet with the Fire Department and Public Works to analyze their internal policies to be sure they are consistent with the Fair Labor Standards law and that the guidelines are closely adhered to.

#### **4. Discussion and possible direction to staff regarding Audit report No. 1108, Tax Audit Assessments and Collections**

Ms. Lisa Gurtler of the City Auditor's Office reviewed the objectives of the audit. The Tax Audit Department is responsible for auditing business operations within Scottsdale to

determine if they are accurately paying transaction privilege sales tax, bed tax, and franchise tax. The City Auditors found that written policies and procedures have been established along with management controls and performance objectives to facilitate compliance with City Code. Opportunities for improvement include reevaluating the mix and utilization of staff. Although the Tax Audit Department is authorized for eight senior audit positions, four of the positions have been filled at lower staff levels. This provides salary savings, but the practice has resulted in higher costs per audit and lower productivity. For example, senior level auditors complete approximately twice as many audits annually than do lower staff levels. Additionally some performance measures have declined during the past three years. Although the Department's goal is to audit at least two percent of Scottsdale businesses annually, the number of businesses audited has declined from 1.7 to 1.4 percent. The collection of tax assessment has continually declined from 65 to 47 percent.

Mr. Phil Montalvo, Tax Audit Manager, commented that it is interesting for auditors to be the subject of an audit. His department is in agreement with the findings, and they are addressing the observations of the audit report. He explained that the higher number of audits completed in the first year the auditors reviewed was due to his department focusing on unlicensed residential rentals. Once those were cleared up, the number of audits completed annually returned to more normal lower levels.

Vice Mayor Klapp asked why the City's collection rate last year was at 47 percent while other cities had much higher rates. Mr. Montalvo said they are currently assessing speculative builders and have assessed over \$1 million, but they have collected about \$800,000. Because of the many bankruptcies, these taxes are hard to collect. The audit compared Scottsdale to Tempe, which is landlocked and has little construction. Every two months the Department meets with the Unified Audit Committee to review standards on optimal recovery rates. He is also working with the Revenue Recovery Manager to determine this.

Vice Mayor Klapp inquired whether they are considering adding another senior auditor, who would be more productive. Since the Department can produce revenue for the City it makes sense to have enough experienced auditors. Mr. Montalvo said with budget constraints it is harder to find a senior auditor, who would likely have been working for another municipality for a number of years. Ms. Walker commented that if the existing positions were filled at the senior auditor level, higher productivity would be required without adding any positions.

Chair Littlefield said the real issue is are they getting everything they should from the current staff. He understands that collection rates drop in an economic downturn and that Scottsdale collection rates will be different than neighboring municipalities. However, he is concerned about the productivity of the Department's existing staff.

Ms. Walker said ensuring development of any auditors or associate auditors to the level of senior auditor is one approach to address the concern. In response to Chair Littlefield's question, Ms. Walker assured that her office will follow up on any staff changes. Mr. Montalvo plans to follow up with the Unified Audit Committee on what other cities are doing and also how they are treating desk reviews, and will report back to the City Auditor.

Vice Mayor Klapp said she felt there would be ways to make desk reviews speedier. Mr. Montalvo said that for speculative building audits, much of the information is already a matter of public record. The tax auditors want to uncover as much information as possible to come to an accurate assessment rather than making adjustments at a hearing. He and one of the senior auditors are looking at what they can do to streamline the information they request, and will work with the City Auditors.

Vice Mayor Klapp asked whether they will get closer to the annual goal of auditing two percent of the businesses by doing this. Mr. Montalvo said they might. The difficulty is that many speculative builders are not licensed, so it is difficult to measure. Adding another senior auditor would get them closer. Currently the less experienced staff are doing a lot of administrative work because the Department lost its full-time administrative secretary three years ago, and then the part-time administrative position was eliminated. He has been talking with the City Manager about sharing an administrative secretary with another department to free up the associate auditors for more audit work. City Treasurer David Smith clarified that though Tax Audit was previously in Finance and Accounting, Mr. Montalvo now reports to the Assistant City Manager.

#### **5. Discussion and possible direction to staff regarding Audit Follow-Up Quarterly Report**

Ms. Walker presented the quarterly report. Divisions are making good progress on about 78 percent of the audit recommendations they are currently tracking. When recommendations that are no longer applicable or not due are eliminated, the implementation status rises to about 94 percent. She noted that the full detailed report is available online; the link is in the cover memo that was attached to the agenda.

#### **6. Discussion and possible direction to staff regarding 2010 Fourth Quarter and Annual TPRO Report**

Ms. Walker presented the Taxpayer Problem Resolution Officer report for the fourth quarter of 2010 and the annual report for the entire year. The report contains data from the previous three years for comparison purposes. Although the response rate is down, the rating result is slightly higher for 2010. No taxpayer complaints or TPRO requests were made in the fourth quarter.

In response to comments from the Committee Members, Ms. Walker said that the managers in the Tax and License and Tax Audit areas have stated they find the taxpayer survey data helpful and that there is a better response rate if the surveys are sent monthly rather than annually. Every business that is audited receives a survey and then a random sample of 60 license holders per month. While the response rate is somewhat low, Ms. Walker said the high levels of satisfaction expressed by respondents suggest that generally people are satisfied; one would expect unhappy taxpayers to be more likely to respond.

**7. Discussion and possible direction to staff regarding status of FY2010/11 Audit Plan**

Ms. Walker reported that staff has completed 11 audits so far and are on track. Audits of Items 18 and 19, Housing programs and Meter Reading respectively, are the only ones they have not yet started.

The contractor expects to complete the Energy Billings audit in February so staff plans to deliver that report in March. She said that the Committee will not need to meet in February unless the Committee members have agenda topics. In reply to a query from Chair Littlefield, Ms. Walker said the Committee is not required to meet every month.

Item 15 is the Benefit Claims audit. That audit is contracted and the cost will be under \$20,000. They expect to deliver a report in May or possibly June.

Ms. Walker summarized that the Department is on schedule.

**8. Discussion of agenda items for the next Audit Committee Meeting (March 21, 2011)**

Ms. Walker announced that staff expects to deliver the report on the energy billings audit. There will also be a preliminary discussion of the FY2011/12 Audit Plan and a budget update.

Mr. Smith said that the City Auditor had wanted to look at the methodology for allocating overhead to the City's enterprise funds. This was deferred from the current year because the City Treasurer's Office wanted to work on a new, fairer allocation methodology. When the new policy is in place for next year, they will welcome the auditors' thoughts.

Chair Littlefield said he looks forward to the new methodology. Mr. Smith outlined the history of charging the enterprises and efforts to come up with a more accurate method to charge for overhead. The new allocation number will be lower than it currently is.

**Public Comment**

No members of the public wished to address the Committee.

**Adjournment**

The meeting adjourned at 4:54 p.m.

Respectfully submitted,  
A/V Tronics, Inc. DBA AVTranz.